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SMALL BUSINESS ADMINISTRATION

13 CFR Part 121

RIN 3245-AG16

Small Business Size Standards; Alternative Size Standard for 7(a), 504, and Disaster Loan Programs

AGENCY: U.S. Small Business Administration.

ACTION: Advance notice of proposed rulemaking.

SUMMARY: SBA is seeking public input to assist in establishing a permanent alternative size standard for its 7(a) and 504 Loan Programs. SBA also invites suggestions on sources of relevant data and information that SBA should evaluate in developing a permanent alternative size standard and assessing its impact. Finally, SBA also seeks input from interested parties on a potential proposal to apply the permanent alternative size standard as an alternative to using industry based size standards for small business applicants under its Economic Injury Disaster Loan (“EIDL”) Program.

DATES: SBA must receive comments to this ANPRM on or before [INSERT DATE 60 DAYS AFTER PUBLICATION IN THE FEDERAL REGISTER].

ADDRESSES: You may submit comments, identified by RIN 3245-AG16 by one of the following methods: (1) Federal eRulemaking Portal: www.regulations.gov, following the instructions for submitting comments; or (2) Mail/Hand Delivery/Courier: Khem R. Sharma, Ph.D., Chief, Office of Size Standards, 409 Third Street, SW, Mail Code 6530, Washington, DC 20416.

SBA will post all comments to this ANPRM on www.regulations.gov. If you wish to submit confidential business information (CBI) as defined in the User Notice at www.regulations.gov, you must submit such information either by mail to the U.S. Small Business Administration, Khem R. Sharma, Ph.D., Chief, Office of Size Standards, 409 Third Street, SW, Mail Code 6530, Washington, DC 20416, or by email to sizestandards@sba.gov. Highlight the information that you consider to be CBI and explain why you believe SBA should hold this information as confidential. SBA will review your information and determine whether it will make the information public. Requests to redact or remove posted comments cannot be honored and the request to redact/remove posted comments will be posted as a new comment.

FOR FURTHER INFORMATION CONTACT: Khem R. Sharma, Office of Size Standards, by phone at (202) 205-7189 or by email at sizestandards@sba.gov.

SUPPLEMENTARY INFORMATION: SBA establishes small business size definitions, commonly known as “size standards,” for private sector industries in the United States to determine eligibility for Federal small business assistance programs, including the SBA’s 7(a) and 504 Loan Programs (“Business Loan Programs”). These size standards are established by 6-digit North American Industry Classification System (NAICS) industry, typically based either on average annual receipts or on average number of employees. SBA uses financial assets and refining capacity to measure the size of a few specialized industries. See, 13 CFR Part 121, Small Business Size Regulations.

On September 27, 2010, the Small Business Jobs Act of 2010 (“Jobs Act”) was enacted (Pub. L. No. 111–240). Section 1116 of the Jobs Act added a new Section 3(a)(5) to the Small Business Act that directed SBA to establish an alternative size

standard using maximum tangible net worth and average net income for applicants of the SBA's Business Loan Programs. The Jobs Act also established for applicants for the SBA's Business Loan Programs a temporary alternative size standard of not more than \$15 million in tangible net worth and of not more than \$5 million in the average net income after Federal income taxes (excluding any carry-over losses) of the applicant for the 2 full fiscal years before the date of the application (referred to as "Interim Rule"), and it provided that this temporary statutory alternative size standard would remain in effect until such time as SBA established a new alternative size standard for the Business Loan Programs through rulemaking. 15 U.S.C. 632(a)(5). Prior to that, SBA had a lower permanent regulatory alternative size standard that applied to the 504 Loan Program, and temporarily applied, for the period beginning on May 5, 2009 and ending on September 30, 2010, to the 7(a) Loan Program. 13 CFR 120.301(b)(2).

On September 29, 2010, SBA issued Information Notice 5000-1175 (available at https://www.sba.gov/sites/default/files/files/bank_5000-1175_0.pdf) providing that, effective September 27, 2010, the new statutory temporary alternative size standard applied to its Business Loan Programs, thereby replacing and superseding the lower existing alternative size standard of \$8.5 million in tangible net worth and \$3 million in average net income, set forth in 13 CFR 121.301(b)(2). The Information Notice further stated that the new statutory alternative size standard would remain in effect until such time as SBA established a permanent alternative size standard for the Business Loan Programs through rulemaking. The Information Notice also stated that SBA's disaster loan program, surety bond guarantee program, small business investment company program, and small business development and contracting programs, as well as other

federal programs utilizing SBA's industry based size standards were not affected by the temporary statutory alternative size standard, and the current standards for those programs in 13 CFR part 121 remained in effect.

Because of the difficulty of obtaining relevant data, SBA has not yet established a new permanent tangible net worth and net income based alternative size standard for its Business Loan Programs, so the Agency continues to use the temporary statutory alternative size standard (referred to in the Jobs Act as the "Interim Rule") to determine eligibility for a small business concern under SBA's Business Loan Programs, in addition to using the industry based size standards. Under the Interim Rule, a Business Loan Program applicant is eligible either under its industry based size standard or if it meets the temporary statutory alternative size standard of \$15 million in tangible net worth and \$5 million in average net income.

SBA is statutorily authorized to provide access to capital to small businesses that do not have credit available elsewhere from non-Federal sources on reasonable terms and conditions. Aiming to expand credit opportunities for small businesses under the distressed credit conditions in the aftermath of the 2007-2009 Great Recession, Congress, through the Jobs Act, temporarily increased by statute the level of the existing regulatory alternative size standard for the Business Loan Programs by raising the maximum thresholds of tangible net worth from \$8.5 million to \$15 million and of average net income from \$3 million to \$5 million, and it provided that the temporary statutory alternative size standard would remain in effect for the Business Loan Programs until such time as SBA established a new permanent alternative size standard.

A review of SBA's internal data on its Business Loan Programs shows that the temporary statutory alternative size standard may have enabled some small businesses that were not otherwise eligible under their industry based size standards to receive 7(a) or 504 Loans ("Business Loans"). However, SBA's internal data systems for its Business Loan Programs lack the necessary detailed electronic data that would allow for an assessment of the exact impact of the Interim Rule on small business loan applicants. Since the Agency's electronic systems only include data regarding the number of employees and the NAICS industry for loan applicants, but not data regarding average annual receipts, tangible net worth or average net income, SBA is not easily able to calculate the exact number of businesses that qualified under the temporary statutory alternative size standard that otherwise could not have qualified under their industry based size standards. Similarly, due to electronic data limitations, SBA cannot easily identify industries or industry sectors in which the temporary statutory alternative size standard helped small businesses the most or the least in accessing SBA Business Loans.

Again, due to the lack of relevant electronic data, SBA is also not in a position to determine whether the Interim Rule is appropriate under the current economic environment or needs to be modified when SBA establishes a permanent alternative size standard.

In an effort to establish a permanent alternative size standard for its Business Loan Programs as mandated by the Jobs Act, SBA has taken steps to gather the information and data necessary to develop an analysis to support the creation of a new permanent alternative size standard based on tangible net worth and average net income. However, the Economic Census data that SBA examines to establish the industry based

size standards does not contain information on tangible net worth or average net income by industry. Furthermore, while SBA collects and maintains limited relevant electronic data on applicants for its Business Loan Programs (such as the number of employees for each loan recipient, but not average annual receipts, tangible net worth, or average net income), SBA's electronic internal data does not show whether an applicant for its Business Loan Programs was determined to be eligible under its industry based size standard or under the alternative size standard. Similarly, the electronic data does not include information on the numbers or amounts of loan approvals that were issued under the industry based size standard or under the temporary statutory alternative size standard.

As such, the only electronic data on size for small business applicants approved for loans through the SBA's Business Loan Programs available for review are the number of employees and the NAICS industry. In an effort to estimate the percentage of loans that were approved under the temporary statutory alternative size standard, SBA examined its electronic internal data on its Business Loan Programs for the three most recent fiscal years (FY 2015 through FY 2017). For this analysis, SBA converted industry based receipts-based size standards to the equivalent number of employees using the receipts-to-employees ratios from the special tabulations of the 2012 Economic Census (<http://www.census.gov/econ/census/>). If the data showed that the number of employees of a loan recipient exceeded its industry based employee size standard (or employee equivalents in the case of receipts-based size standards), SBA deemed for the purposes of this analysis that the loan was approved under the temporary statutory alternative size standard. Conversely, if the loan recipient's number of employees was

equal to or less than the industry based size standard, it was deemed for the purposes of this analysis that the loan could have been approved under the industry based size standard.

Based on the results obtained from this analysis, SBA estimates that about 1.3% of the 207,161 total loan approvals issued during FY 2015-2017 went to firms that exceeded their industry based size standard, thereby implying that these firms were most likely qualified only under the temporary statutory alternative size standard. SBA estimates the total value of these loans to be \$3.1 billion, or 3.6% of \$86.9 billion in total loans approved during that period. Such a small percentage of loan approvals issued to firms that exceeded their industry size standard (1.3%) suggests that a vast majority of small businesses receiving loans through SBA's Business Loan Programs would have qualified under their industry based size standards and would not be impacted significantly by a modification, if any, to the Interim Rule.

Although useful, the analyzed data is selective in that it includes only those firms that were approved for and received an SBA Business Loan, but not those that applied and were not approved nor those interested in applying in the future. This data does not allow SBA to accurately determine the broader impact of a change to the Interim Rule, nor does it provide the Agency with a robust source of information from which a new permanent alternative size standard can be developed. Furthermore, while SBA has approximated the percentage of all loan approvals issued to small businesses that qualified only under the Interim Rule, it is not possible to determine the precise impact because the available electronic data lacks tangible net worth and average net income data for the impacted population of small businesses. Data on tangible net worth and

average net income for the impacted businesses, if available from other sources, may reveal additional insights into the results of SBA's analysis of FY 2015-2017 loan data.

Additionally, SBA is statutorily authorized to make direct loans under the EIDL Program to small businesses that do not have credit available elsewhere and that have suffered a substantial economic injury as a result of a disaster. 15 U.S.C. 636(b)(2). Historically, the size standards applicable to small business concerns that apply for loans under the EIDL Program have been the same industry based size standards applicable to small business applicants for the Business Loan Programs. See, 13 CFR 123.300(b). Although the temporary statutory alternative size standard established by the Jobs Act does not apply to the EIDL Program, SBA is considering applying the new permanent alternative size standard established for the Business Loan Programs to the EIDL Program as an alternative to industry based size standards.

Request for Comments

Against the above backdrop, in this ANPRM, SBA seeks comment on the following issues.

1. SBA seeks comment on whether or not the level of the temporary statutory alternative size standard under the Interim Rule (i.e., \$15 million in tangible net worth and \$5 million in average net income) is appropriate under the current credit environment and as a new permanent alternative size standard. Commenters in support of the level in the Interim Rule should provide justification, along with supporting data and analysis to support their position. Similarly, commenters who believe the level established in the Interim Rule is not appropriate as a permanent alternative size standard should suggest,

along with supporting data and analysis, a different alternative size standard which they believe would be more appropriate. The suggested alternative size standard must be based on tangible net worth and average net income as required by section 3(a)(5) of the Small Business Act. 15 U.S.C. 632(a)(5).

2. SBA seeks comment on the impact of using an alternative size standard on small businesses seeking loans through its Business Loan Programs. Specifically, SBA welcomes information on industries/sectors where small businesses benefit the most or do not benefit at all from the use of an alternative size standard. Similarly, SBA is also looking for data on the number of businesses approved for SBA's Business Loans under the temporary statutory alternative size standard that otherwise could not have been approved under their industry based size standards.

3. SBA invites suggestions on sources of relevant data and information, especially tangible net worth and average net income of applicants to SBA's Business Loan Programs, that SBA can evaluate to assess the impact of the Interim Rule on small businesses and use in developing a new permanent alternative size standard and in estimating the impact of the new permanent alternative size standard.

4. SBA invites comments from interested parties on the proposal to apply the same new permanent alternative size standard established for the Business Loan Programs to the EIDL Program as an alternative to industry based size standards.

5. SBA also seeks comment on how the Interim Rule has affected the processes used by lenders participating in the Business Loan Programs and what effects a permanent alternative size standard would have on application processes and processing times.

6. SBA invites comment on the effects of the Interim Rule on conventional small business lending. Specifically, SBA welcomes input on whether, and to what extent, if any, SBA Business Loans approved under the Interim Rule have substituted for or displaced directly or indirectly conventional small business lending, or whether such SBA Business Loans played more of a supplementary role in conventional small business lending activity.

Dated: March 14, 2018.

Linda E. McMahon,
Administrator.

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